COMPETITION & MARGINAL ANALYSIS

GROUP 3

Aarathi L R, A18 | IES

Abhijeet Bansode, A15 | IPoS

Ashutosh Singh, A16 | IPS

Pankaj Kumawat, B62 | IPS

Rohit Naagar, A14 | ISS

Saumya Sakshi, A11 | ISS

Suman W M Sivachar, B38 | IFS

Vasundhara Gulhane, A18 | IPoS

CONTENTS

- Competition – *crucial in price determination*
  - Market Structure
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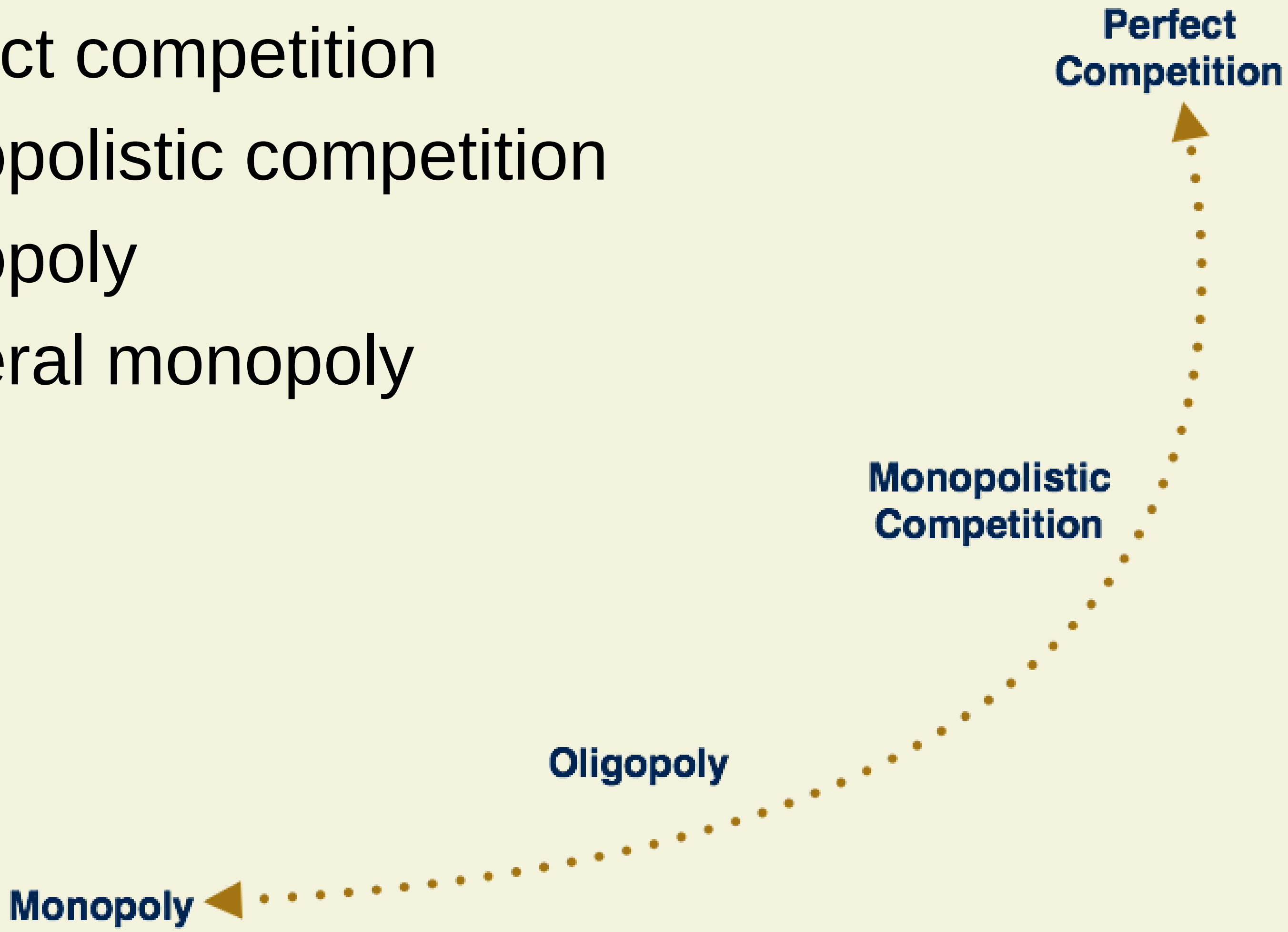
- Marginal & Incremental Analysis - *marginalism over incrementalism*
- References

COMPETITION

It’s nice to have a valid competition; it pushes you to do better
Gianni Versace

MARKET STRUCTURE

- Perfect competition
- Monopolistic competition
- Monopoly
- Bilateral monopoly



PERFECT COMPETITION

- Characterized by the complete absence of rivalry

Assumptions

- Large number of buyers and sellers – cannot affect the price by changing the supply
- Product homogeneity-graph - demand curve infinitely elastic: AR=MR=P
- Free entry and exit of firms
- Profit maximization
- No government regulation

AR (Average Revenue) =
MR (Marginal Revenue) =
P (Price)

III PERFECT COMPETITION

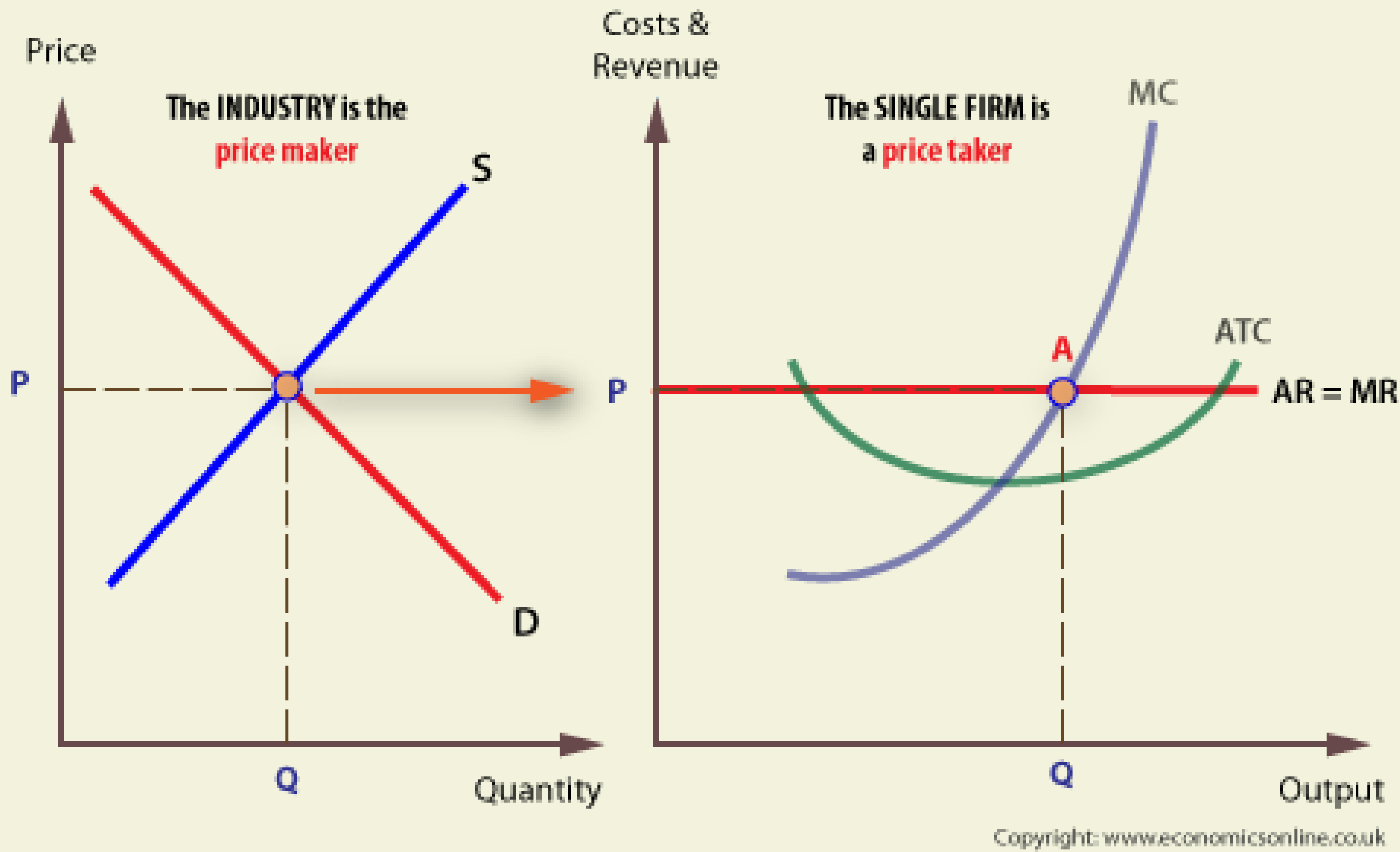
EQUILIBRIUM OF THE FIRM

MC (Marginal Cost) = MR (Marginal Revenue)

Slope of MC > Slope of MR

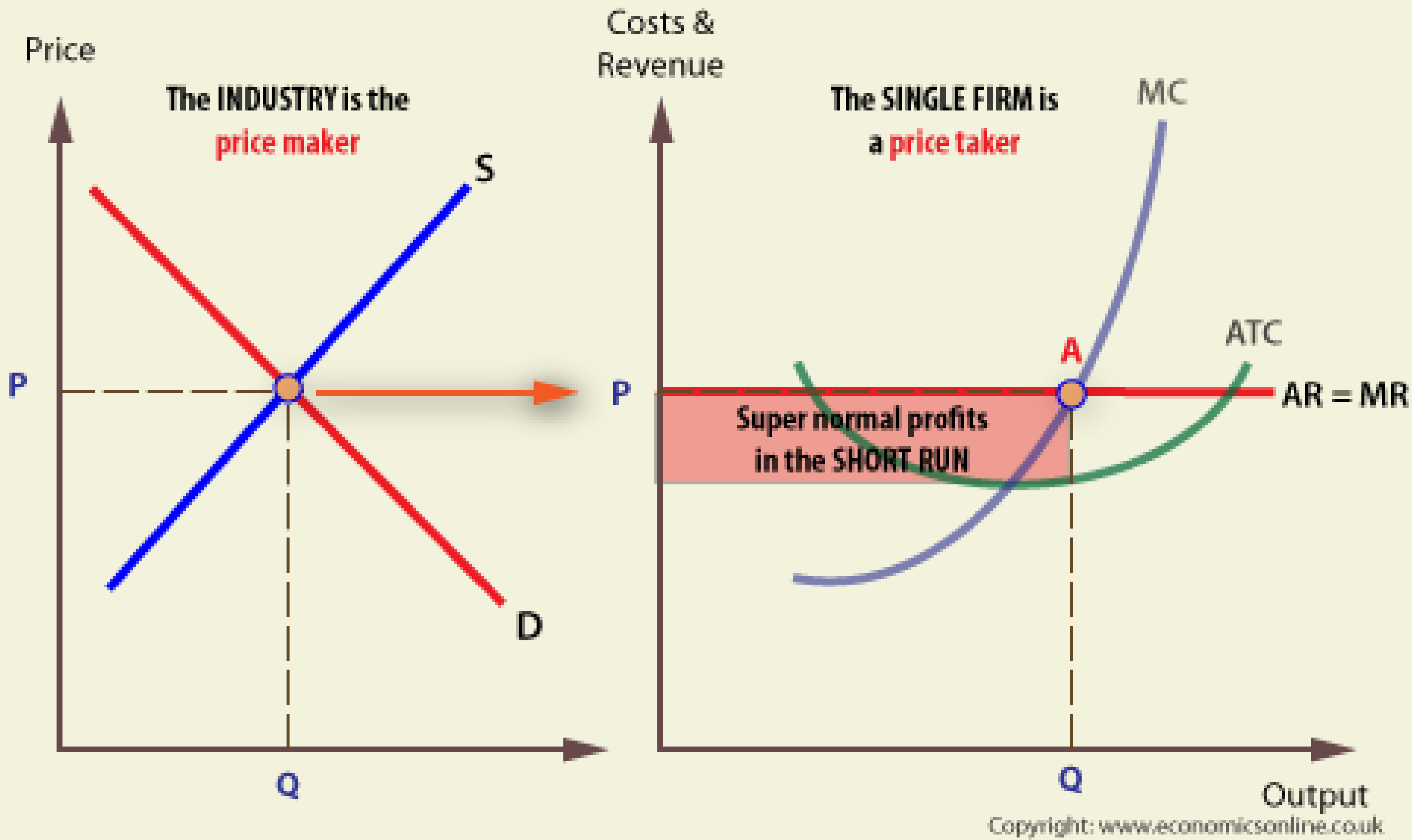
PERFECT COMPETITION

The Firm as a Price Taker



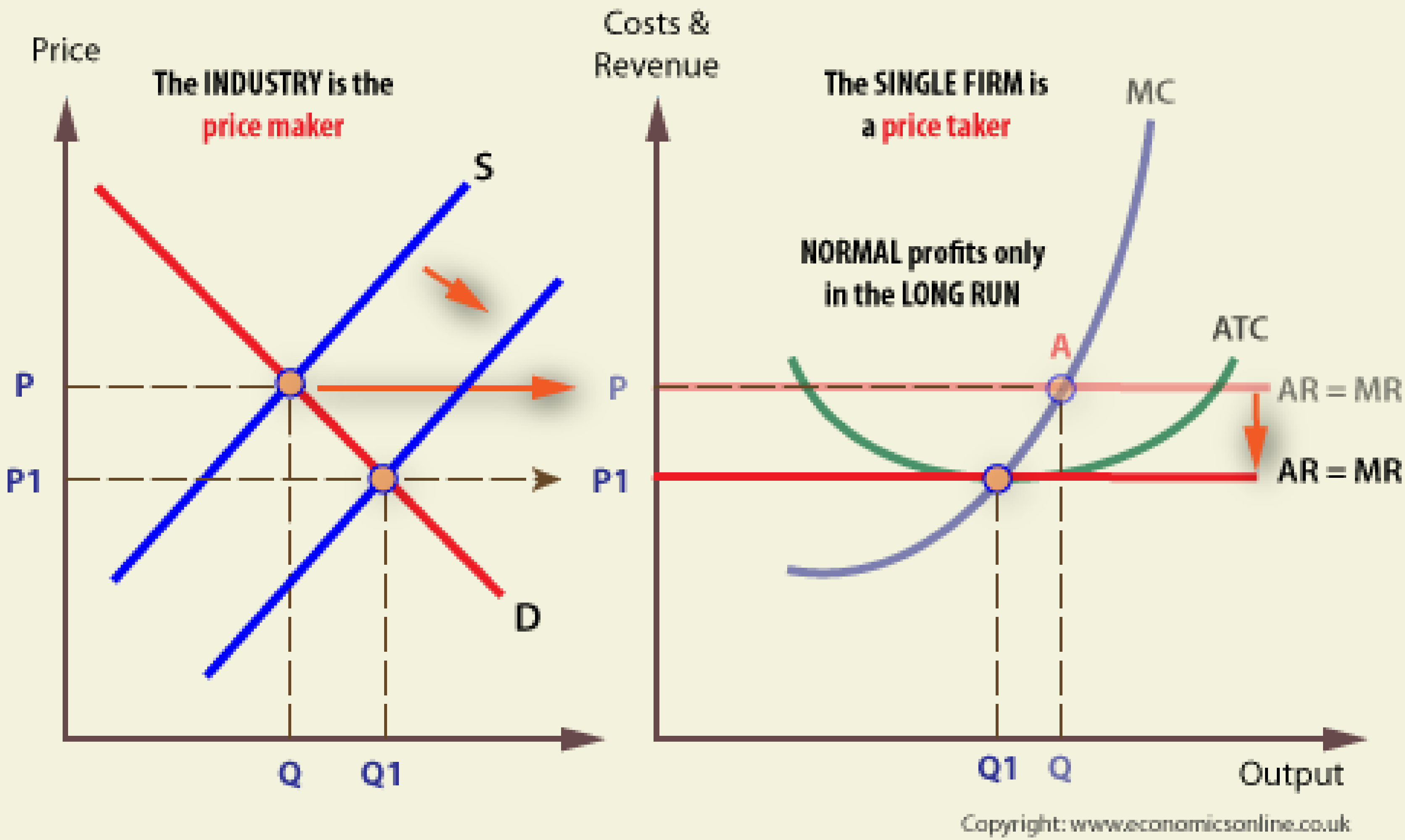
III PERFECT COMPETITION

In the Short Run



PERFECT COMPETITION

In the Long Run

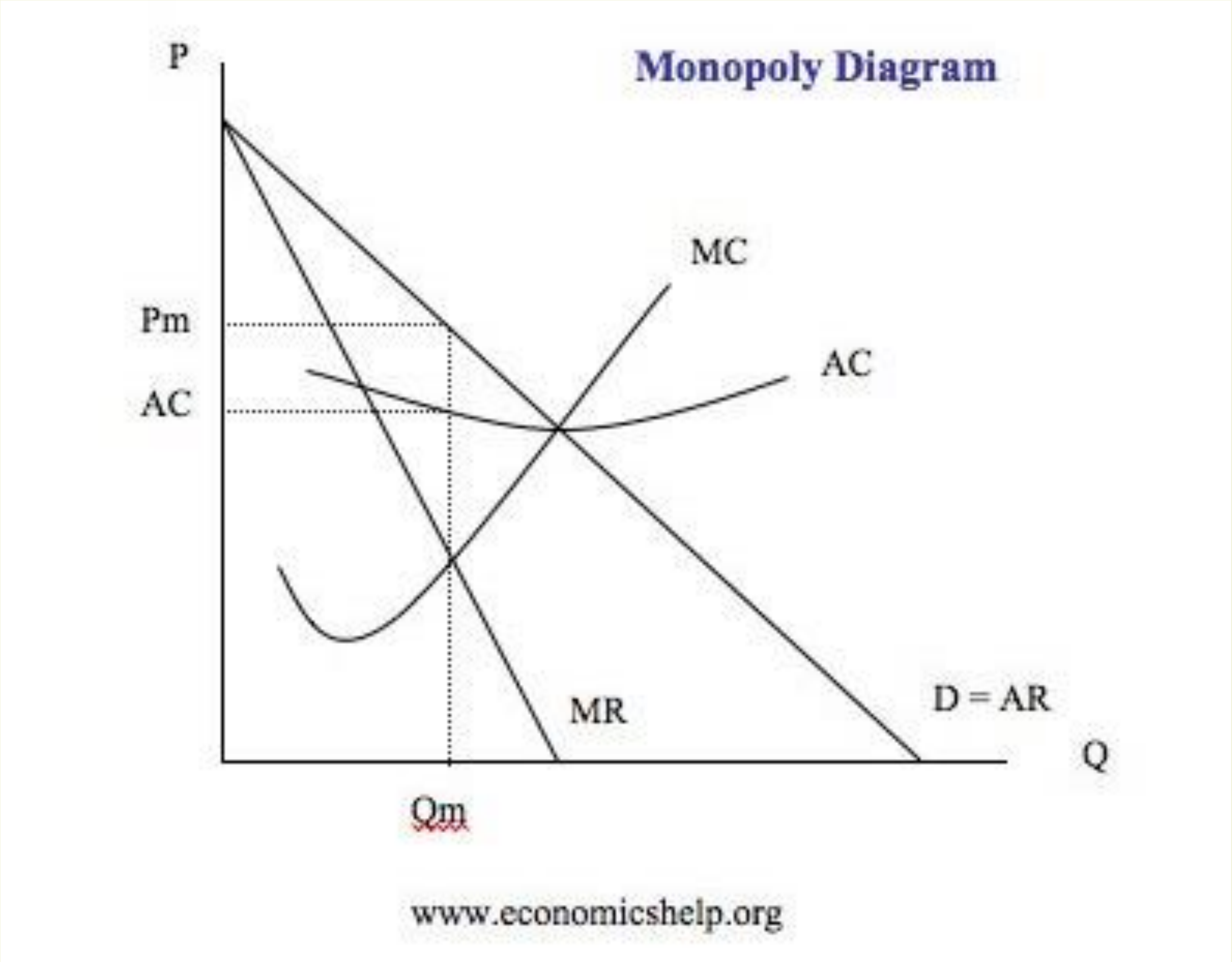


MONOPOLY

- Single seller
- No close substitutes for the commodity
- Barriers to entry

- Government regulations e.g.
  - Patents, copyrights and licensing
  - Natural monopoly

MONOPOLY


Monopoly Diagram
P
Pm
AC
MC
AC
MR
D = AR
Q
Qm
www.economicshelp.org

MONOPOLISTIC COMPETITION

- Large number of buyers and sellers
- Differentiated products, yet they are close substitutes
- Free entry and exit of firms
- Profit maximization
- Firm has limited control on price determination

E.g. cloth stores, shoes, furniture

BILATERAL MONOPOLY

- Market consisting of single seller and single buyer

E.g. Indian Airlines – IOC (before 1991)

OLIGOPOLY

- market consisting of few sellers

E.g. OPEC

MARKET STRUCTURE

Extent of competition plays a very important role in PRICE determination

INTERNATIONAL TRADE

INTERNATIONAL TRADE

Basis

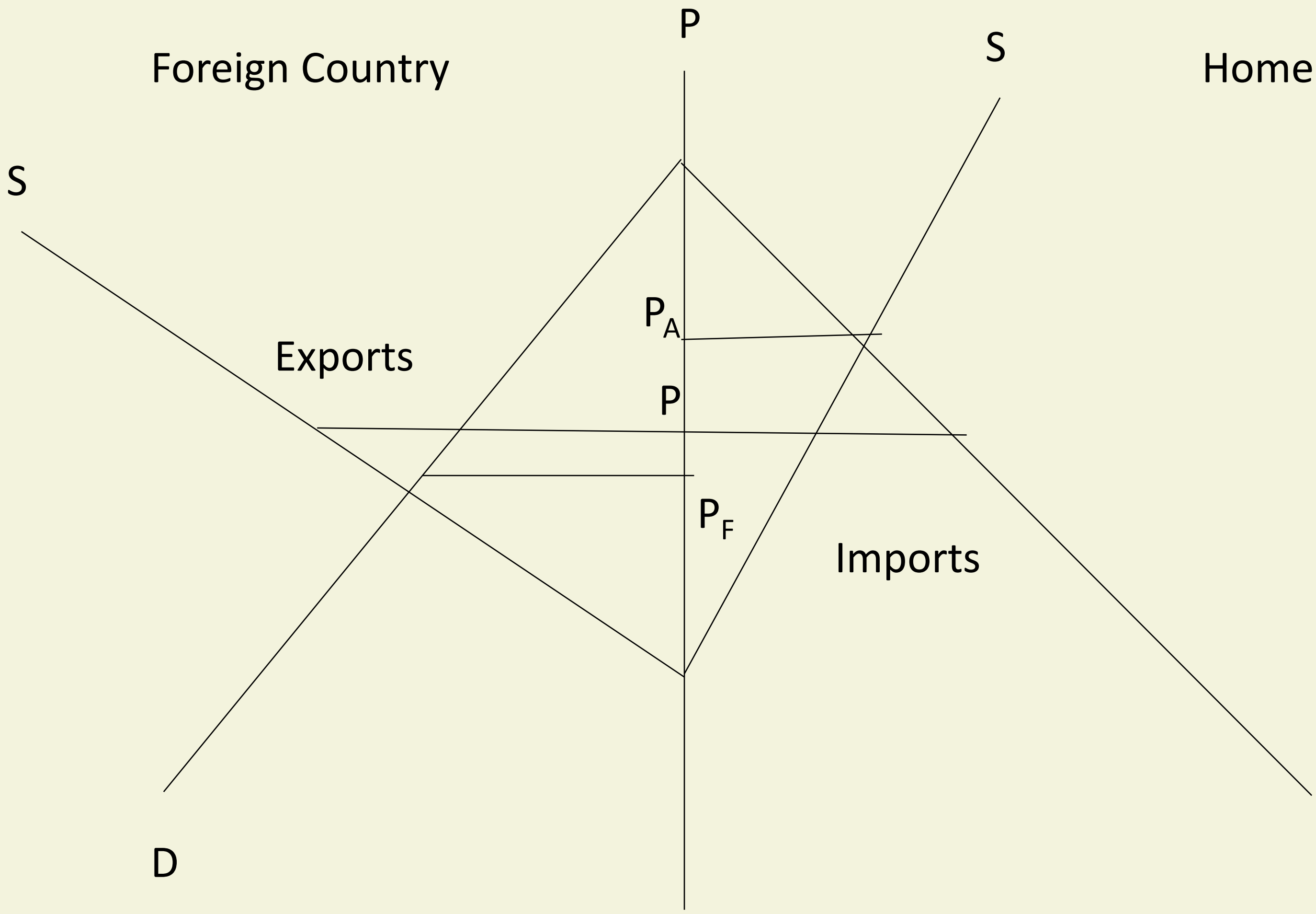
Gains to be made from exchange of goods and services

Immediate cause

Differences in price of goods and services between countries

- Trade widens the market - brings in competition - more competitive price
- Source
  - comparative cost advantage
  - comparative price advantage
  - different factor endowments
  - E.g. Non-availability of resources

INTERNATIONAL TRADE



WTO

- A regulatory body to oversee a fair and free competition and trade practices between nations
- Looks into
  - Trade negotiations
  - Dispute resolution

ANTI-TRUST LAWS

- Sherman Act 1890, USA
- Clayton Act 1914, USA
- Competition Act 2002, India & Competition Commission of India

INTERNATIONAL TRADE

- OPEC cartel
- De beers diamond prices monopoly
- Banana wars
- Microsoft
- Small weapons – duopoly
- Too big to fail banks - Banking in recession

DE BEERS CASE STUDY

- Big monopoly
- Till 2000, only company to control 80% of the suppliers

DOMESTIC UNFAIR PRACTICES

- Coal India Limited
- DLF

RGINALISM & INCREMENTALISM

MARGINALISM & INCREMENTALISM

Marginal Principle

- Defined in terms of unit changes
- Reference to one independent variable
- An important concept in economics

Incremental Principle

- Defined in terms of bulk changes
- More than one independent variable can be considered at a time
- Important in decision making

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ATTRIBUTIONS


Thank you.